**Attachment 2**

WILSHIRE CONSULTING

*Michael C. Schlachter, CFA*
*Managing Director*

June 3, 2007

Dr. Russell Read
Chief Investment Officer
California Public Employees' Retirement System
400 P Street, Suite 3492
Sacramento, CA 95814

Re: Inflation-Linked Asset Class

Dear Russell,

You requested Wilshire's opinion regarding Staff's proposal for implementation of the new inflation-linked asset class, pending approval by the Investment Committee and the asset allocation review in November. We recognize that this is not entirely new ground, as some of the assets to be included in this asset class already exist within CalPERS, and therefore does not require as much ground level preparation and education to launch this investment portfolio. On the other hand, we also recognize that the creation of a new asset class within CalPERS, complete with SIO and dedicated Staff is an affair that should not be undertaken lightly. Furthermore, we remind you and the Investment Committee that the amount of any investment in this new asset class will be determined as part of the asset allocation study in November, and the possibility remains that there might be no investment at all in this asset class.

As you are well aware, in its capacity as General Pension Consultant, Wilshire was the natural candidate to work with Staff in developing this new asset class, and we have worked closely with you and your team throughout the workshop last Summer, the commodities pilot program, and now this presentation. We expect that we will continue to work with you and your Staff through the balance of the year as the construction of this new asset class reaches fruition.

As stated above, the four investment types to be included in this new asset class already exist in CalPERS' portfolio presently, and have been previously reviewed and approved by the Investment Committee for investment elsewhere within the PERF. Inflation-linked bonds are issued by governments or investment grade companies, and are already permitted within the internal fixed income portfolio. Timberland has been permitted in the Real Estate portfolio for some time. Commodities were approved as a pilot program in the Fall of 2006. Infrastructure is the one investment type where it could be argued that CalPERS will be breaking new ground. Some investments that could be called infrastructure have appeared over the years in CalPERS' Real Estate and AIM portfolios, but this will be the first dedicated investment program in this area. Nonetheless, CalPERS' existing Real Estate and AIM Staff, plus some additional personnel who have yet to be hired, have the expertise necessary to implement this investment.

We believe that all four proposed investment types qualify as inflation-linked assets to a greater or lesser extent. Inflation-linked bonds provide the purchaser with perhaps the most perfect inflation hedge, since the change in return on the bonds is determined by the inflation rate. Investments in commodities and timber will reflect directly changes in the cost of some raw materials, which are included in some measures of inflation. Infrastructure has the least strong link to inflation of the four, since returns to infrastructure can be impacted by future changes in usage of the asset in question (i.e., greater use of alternative fuels could decrease the return on investment in certain types of power facilities, technological advances or demographic changes could impact future returns on transportation infrastructure investments.) However, given the fact that returns on infrastructure investments over time are derived from increases in demand from population growth and from moderate pricing power similar to inflation, we see no reason to exclude infrastructure from this asset class.

Staff has proposed an initial mix of the four investment types, based on some preliminary work. Wilshire feels that this allocation is appropriate given the market size and characteristics of each of the investment types. We note that this has been a valiant effort by Staff to determine the appropriate mix of investment types based on a variety of factors, including liquidity, market size, likely return and risk, and diversification advantages, however we note that this mix will possibly change over time as CalPERS gains experience in this area and as asset-allocation Staff are hired who bring new expertise to CalPERS that guides this investment program in a different direction than what has been proposed.

We also note that Staff has significant work left to complete, including the hiring of an asset-allocation SIO and associated Staff, development of policy language governing this asset class, and development of incentive compensation measures for asset-allocation Staff, and we look forward to working with you, your Staff, and the Investment Committee over the next few quarters as we move closer to potentially having dedicated investments in these areas.

If you have any additional questions, please do not hesitate to contact me.

Sincerely,